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FILED
FEB 9 1942
CHARLES ELMORE CROPLEY
CLERK

In the Supreme Court
OF THE
United States

OCTOBER TERM, 1941

No. 934

NELSON TAYLOR, J. R. MASON, GILBERT MOODY, and N. O. BOWMAN,
Petitioners,

vs.

PROVIDENT IRRIGATION DISTRICT,
Respondent.

PETITION FOR WRIT OF CERTIORARI
to the United States Circuit Court of Appeals
for the Ninth Circuit
and
BRIEF IN SUPPORT THEREOF.

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PETITION FOR WRIT OF CERTIORARI
to the United States Circuit Court of Appeals
for the Ninth Circuit.

To the Honorable Harlan F. Stone, Chief Justice of the United States, and to the Associate Justices of the Supreme Court of the United States:

Petitioners pray that a writ of certiorari issue to review the decision (R. 234) of the Circuit Court of Appeals of the Ninth Circuit made in the above entitled cause on December 4, 1941, which affirmed the

interlocutory decree of the District Court of the Northern District of California, Northern Division, rendered against petitioners on January 21, 1941. (R. 200.)

OPINIONS BELOW.

Opinion of the Circuit Court of Appeals, ... Fed. (2d) ..... (R. 234.)

JURISDICTION.

The decision in the Circuit Court of Appeals was rendered December 4, 1941. (R. 234.) The mandate was stayed until disposition of the case by this Court. (R. 244.) The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code (28 U. S. C., paragraph 347 (a)).

STATUTES INVOLVED.

Municipal Bankruptcy Act of May 24, 1934, c. 345 (48 Stat. 798), 11 U. S. C. 301-303, adding Sections 78-80 to the Bankruptcy Act of 1898; Act of August 16, 1937, c. 657 (50 Stat. 654), 11 U. S. C. 401-404, adding Sections 81-84; and Act of June 22, 1938, c. 575, Sec. 3 (b) (52 Stat. 940). Principal California statutes involved are "the California Irrigation District Act", Cal. Stat. 1897, p. 254 as amended; the "California Districts Securities Commission Act", Cal. Stat. 1931, p. 2263 as amended.

SUMMARY STATEMENT OF THE MATTER INVOLVED.

This is a proceeding brought by the respondent Provident Irrigation District, a California irrigation district, for confirmation of composition of debts under Chapter IX of the Bankruptcy Act of 1898 as amended. (11 U. S. C. Sec. 401-404.)

The matter came on before the Court for hearing on November 18, 1940 on the petition filed by the Provident Irrigation District, hereinafter called the district, the petition having been filed May 29, 1940, and the answer and objections to the petition.

The district, a state agency, was organized in 1918 pursuant to the California Irrigation District Act (Cal. Stat. 1897, p. 254, as amended), is located in the counties of Glenn and Colusa in California, and comprises approximately 22,805 acres. In 1918 the district issued a first issue of general obligation coupon bonds in the amount of $1,000,000 and in 1921 a second issue of $190,000, all bearing interest at 6%. Present outstanding indebtedness is $957,000. At the time of the hearing $341,000 of this amount had matured and interest coupons in the amount of $415,192.50 had matured and were unpaid. Total outstanding indebtedness of the district was $1,400,672.50. The district applied to the Reconstruction Finance Corporation for a loan and on December 20, 1939, was granted such in the amount of $193,500. The plan offered to the bondholders 20 cents for each dollar of unpaid principal amount of the old bonds, plus the full amount of any interest coupons prior to July 1, 1931. The terms of the loan provided among other things that the district

was to reduce its size to approximately 13,000 acres. The petitioners have resisted the plan and the proceedings in the courts relative thereto, and own principal of bonds as follows: Nelson Taylor $3000; J. R. Mason $17,000; Gilbert Moody $3000; N. O. Bowman $9000.

The Nelson Taylor bonds matured August 15, 1930 and were presented for payment January 30, 1931 but not paid. Other bonds, later in maturities and presentations, were paid in full. Taylor's bonds, due in 1930 were evidently not paid because the district took the erroneous position that they were "outlawed". (R. 181.) There are no other unpaid bonds of the 1930 maturity.

The fiscal agent for the district was to receive $20,-300 for his services. (R. 123.)

The Bankruptcy Act (Sec. 403 (e)), provides that a plan may be confirmed if "(1) it is fair, equitable, and for the best interests of the creditors and does not discriminate unfairly in favor of any creditor or class of creditors; (2) complies with the provisions of this chapter; (3) has been accepted and approved as required by the provisions of subdivision (d) of this section; (4) all amounts to be paid by the petitioner for services or expenses incident to the composition have been fully disclosed and are reasonable; (5) the offer of the plan and its acceptance are in good faith; and (6) the petitioner is authorized by law to take all action necessary to be taken by it to carry out the plan."

Also, that "(i) Nothing contained in this chapter shall be construed to limit or impair the power of any

State to control, by legislation or otherwise, any municipality or any political subdivision of or in such State in the exercise of its political or governmental powers, including expenditures therefor."

Our view of the case.

The plan of composition provides for the payment of obligations of the district maturing up to and including January 1, 1931 in full, but does not provide for the payment in full of the bonds of Nelson Taylor, amounting to $3000 which matured August 15, 1930, and which the district admittedly should have paid prior to filing in bankruptcy.

Other bonds of the same and later maturities and presentations were paid in full. (R. 118, 181, 189.) Many interest coupons of later presentations than Taylor's bonds were paid in full, and in fact the plan is that all coupons of January 1, 1931 maturity are to be paid in full. This is directly contrary to *Bates v. McHenry,* 123 Cal. App. 81, and *Provident Land Corp. v. Zumwalt,* 12 Cal. (2d) 365,[1] which held that payment must be in order of presentation. At the time of the latter case, the district had a "surplus" of $10,000 (R. 179), and under the law as declared by the highest court of California payment should have been made to Taylor from that money before any bonds or interest coupons of later presentations were paid. At the time of the bankruptcy hearing, the district had that $10,000 and also $5500 in redemption money. The "plan" wholly disregards this right by

[1]This case is set forth in the Appendix p. i, substantially in full.

providing for payment in full of all January 1, 1931 interest coupons regardless of their later maturity and regardless of their dates of presentation for payment. The record indicates (R. 67) that most of the January 1, 1931 coupons are in the hands of one man. This should have prompted an inquiry under the rule of *Roberts v. Board of Public Instruction,* 117 Fed. (2d) 943.

But the essential fact is that Nelson Taylor's bonds through error or deliberately were not paid prior to the bankruptcy petition. They admittedly should have been so paid. The bankruptcy petition and decree do not right this wrong but condone it. Equity and right could be done and should be done.

The case of *Moody v. Provident Irrigation District,* 12 Cal. (2d) 389, in effect holds that after presentation for payment bond obligations of California irrigation districts are not due until funds are on hand available for payment. The bonds involved in that case are the same held in this case by Moody. The district is therefore able to meet its debts as they mature and the inability required by Bankruptcy Act, Section 403 (a) is not present.

In *Provident Land Corp v. Zumwalt,* Appendix p. i, the Supreme Court of California, with reference to this district, said that the land of this district can never be released from the obligation of its bonds until they are paid and that the district only exercises its powers as a trustee for the payment of these obligations. There were only three resident landowners in

the district and therefore nearly all the land of the district is to be held and operated exclusively for the benefit of the bondholders. The court below ignored this declaration of law as to this district.

The *Provident* cases referred to are not only statements of general law applicable to this field, but are adjudications of the facts and law pertaining to this particular district. In passing upon a plan of composition, a bankruptcy court is bound by local law. (*Ginsberg v. Lindel,* 107 Fed. (2d) 721, 725, 726; *American United Mutual Life Ins. Co. v. City of Avon Park,* 108 Fed. (2d) 1010, 61 S. Ct. 157.)

The arrangement to pay the fiscal agent of the district $20,300 is unreasonable in that it is more than 10% of the amount paid to the bondholders.

The district was not shown to be authorized by law (Bankruptcy Act, Sec. 403 (e) (6)) to exclude approximately 10,000 acres under Sections 74 to 84 of the California Irrigation District Act. This land has an apparent value of $7 an acre to the Biological Survey, but the landholders receive nothing from it.

The district has sold 46 parcels of land, 11,294.49 acres, for nearly $10 an acre or approximately $112,000. This money was properly payable to bondholders, since the land was taken by the district for non-payment of taxes, but instead was used to relieve the lands of Reclamation District and county taxes, and to pay interest coupons to January 7, 1931 in full. (R. 104.)

Under the California law, and by practice among the districts, irrigation districts can and this district

does exclusively rent its land to tenants. This practice is more beneficial to the bondholders than sale which produces nothing for the bondholders.

The Bankruptcy Act requires a comparison of total assets to liabilities. (*Cusick v. Second Nat. Bank,* 115 Fed. (2d) 150.) But the district produced no appraisals, no land valuations, no valuations of district property, nor a statement of income and expenditures since its default. No balance sheet or statement of capital assets or income, or financial history was produced. The only evidence on the ability of the district was that of two or three witnesses who were of the opinion the plan is fair.

QUESTIONS PRESENTED.

1. May creditors subsequent in right of payment secure full payment as against 20% payment to one having a vested prior right to payment in full?

2. May a court of bankruptcy disregard the local law applicable to a state agency, declared by the highest court of California?

3. May a court of bankruptcy refuse to follow the facts and law pertaining to this particular district determined and stated by the highest court of California?

4. Is payment of $20,300 to a fiscal agent of a district, such amount being more than 10% of that to be paid to bondholders, reasonable?

5. Is exclusion of land (worth $50,000 to $70,000 and held in trust for bondholders) with no benefit to district or bondholders, fair and equitable?

6. Does approval of a plan of composition require evidence of assets and liabilities, and earning capacity or is mere opinion evidence that it is fair sufficient?

REASONS FOR GRANTING WRIT OF CERTIORARI.

(1) The courts below in this case have decided important questions of law conflicting with local decisions.

The Supreme Court of California in *Provident Land Corp. v. Zumwalt,* supra, decided that bonds of the Provident Irrigation District must be paid in the order of their presentation for payment. In this case the courts below have held that bond obligations later in maturity and presentation for payment should be paid in full while those earlier are to be paid at the rate of 20%. In doing so the bankruptcy court condoned an admitted act of wrongdoing by the district, when it could have righted this wrong by a conditional decree requiring payment in full of Taylor's claim.

The Supreme Court of California decided in *Moody v. Provident Irrigation District,* supra, that bonds of the Provident Irrigation District are not due until funds are available for their payment. In this case the lower courts have held that the Provident Irrigation District is unable to meet its obligations as they mature because it does not have sufficient money on hand.

The Supreme Court of California, in *Provident Land Corp. v. Zumwalt,* Appendix p. i, decided that nearly all the lands of the district are owned by the district and are held by the district in trust, the bondholders being a beneficiary of that trust, and that the land "can never be permanently released from the obligation of the bonds until they are paid". In this case the lower courts have held that the district may secure a loan on the land and remove this trust property from the bondholders, and terminate the bondholders' right to further payment.

(2) The lower courts have decided important questions in conflict with the weight of authority.

The *Erie Railroad v. Tompkins* case, 304 U. S. 64, requires federal courts to follow the law as stated by the state courts.

The cases of *Consolidated Rock Products Company v. Du Bois,* 312 U. S. 510, and *Case v. Los Angeles Lumber Products Co.,* 308 U. S. 106, require evidence and findings on the fairness of a plan based on the assets and earning capacities of a debtor. This should be particularly true of a trust relationship such as we have here, yet the record is without such evidence.

The case of *American Un. Mut. Life Ins. Co. v. City of Avon Park,* 311 U. S. 138, requires inquiry into and reasonableness in payments of fees and expenses in connection with reorganization and composition matters.

Further, settled principles of law require that questions once determined by a court cannot be again ques-

tioned. The doctrine of *res judicata* requires the bankruptcy court to follow the facts and law stated by the Supreme Court of California in the cases referred to which involved this district.

(3) The lower courts have decided an important question of federal law which has not been but should be settled by this Court, this question being whether or not the bankruptcy power extends to reversal of trust declarations made by highest state courts.

(4) The lower courts have decided federal questions in conflict with decisions of this Court.

They have not followed the *Erie Railroad v. Tompkins* case by failure to give effect to the decisions of the Supreme Court of California.

They have disregarded an unreasonable payment made to a fiscal agent contrary to *American Un. Mut. Life Ins. Co. v. City of Avon Park,* supra.

They have given unlawful preference to certain creditors in disregard of principles stated by this Court in *Case v. L. A. Lumber Products Co.,* supra, and *Consolidated Rock Products Co. v. Du Bois,* supra.

Wherefore, petitioners pray that a writ of certiorari be issued out of and under the seal of this Honorable Court, directed to the United States Circuit Court of Appeals for the Ninth Circuit, commanding that Court to certify and to send to this Court for its review and determination a full and complete transcript of the record and of the proceedings of said Court in the case numbered and entitled

in its dockets as "No. 9809, Nelson Taylor, J. R. Mason, Gilbert Moody, and N. O. Bowman, Appellants, v. Provident Irrigation District, Appellee", and that the decree of said Court be reversed by this Court with directions to dismiss the bill, and for such other relief as to this Court may seem proper.

Dated, Turlock, California,
February 2, 1942.

NELSON TAYLOR,
J. R. MASON,
GILBERT MOODY,
N. O. BOWMAN,
Petitioners.

W. COBURN COOK,
Counsel for Petitioners.